

On August 20, 1970, M has accounts receivable, arising from the sale of tools, amounting to \$5,000. Under local law, X's security interest arising by reason of the \$10,000 advance on August 3, 1970, has priority, with respect to the raw materials and accounts receivable, over a judgment lien against M arising July 6, 1970 (the date of tax lien filing) out of an unsecured obligation.

(ii) Because the \$10,000 advance was made before the 46th day after the tax lien filing, and the accounts receivable in the amount of \$5,000 and the raw materials were acquired by M before such 46th day, X's \$10,000 security interest in the accounts receivable and the inventory has priority over the tax lien. The priority of X's security interest also extends to the proceeds, received on or after the 46th day after the tax lien filing, from the liquidation of the accounts receivable and inventory held by M on August 20, 1970, if X has a continuously perfected security interest in identifiable proceeds under local law. However, the priority of X's security interest will not extend to other property acquired with such proceeds.

Example 2. Assume the same facts as in example 1 except that on July 15, 1970, X has actual knowledge of the tax lien filing. Because an agreement does not qualify as a commercial transactions financing agreement when a disbursement is made after tax lien filing with actual knowledge of the filing, X's security interest will not have priority over the tax lien with respect to the \$10,000 advance made on August 3, 1970.

Example 3. Assume the same facts as in example 1 except that, instead of additional inventory, on August 5, 1970, M acquires an account receivable as the result of the sale of machinery which M no longer needs in his business. Even though the account receivable was acquired by taxpayer M before the 46th day after tax lien filing, the tax lien will have priority over X's security interest arising in the account receivable pursuant to the earlier written agreement because the account receivable was not acquired by the taxpayer in the ordinary course of his trade or business.

Example 4. Pursuant to a written agreement with the N Manufacturing Company entered into on January 4, 1971, Y a commercial factor, purchases the accounts receivable arising out of N's regular sales to its customers. On November 1, 1971, in accordance with § 301.6323(f)-1, a notice of lien is filed with respect to N's delinquent tax liability. On December 6, 1971, Y, without actual notice or knowledge of the tax lien filing, purchases all of the accounts receivable resulting from N's November 1971 sales. Y has taken appropriate steps under local law so that the December 6, 1971, purchase is protected against a judgment lien arising November 1, 1971 (the date of tax lien filing) out of an unsecured obligation. Because the pur-

chaser of commercial financing security, other than inventory, is treated as having acquired a security interest in commercial financing security, and because Y otherwise meets the requirements of this section, the tax lien is not valid with respect to Y's December 6, 1971, purchase of N's accounts receivable.

[T.D. 7429, 41 FR 35503, Aug. 23, 1976]

§ 301.6323(c)-2 Protection for real property construction or improvement financing agreements.

(a) *In general.* Even though a notice of a lien imposed by section 6321 is filed in accordance with § 301.6323(f)-1, the lien is not valid with respect to a security interest which:

(1) Comes into existence after the tax lien filing,

(2) Is in qualified property covered by the terms of a real property construction or improvement financing agreement entered into before the tax lien filing, and

(3) Is protected under local law against a judgment lien arising, as of the time of tax lien filing, out of an unsecured obligation.

For purposes of this section, it is immaterial that the holder of the security interest had actual notice or knowledge of the lien at the time disbursements are made pursuant to such an agreement. See paragraphs (a) and (e) of § 301.6323(h)-1 for general definitions of the terms "security interest" and "tax lien filing." For purposes of this section, a judgment lien is a lien held by a judgment lien creditor as defined in paragraph (g) of § 301.6323(h)-1.

(b) *Real property construction or improvement financing agreement.* For purposes of this section, the term "real property construction or improvement financing agreement" means any written agreement to make cash disbursements (whether or not at the option of the party agreeing to make such disbursements):

(1) To finance the construction, improvement, or demolition of real property if the agreement provides for a security interest in the real property with respect to which the construction, improvement, or demolition has been or is to be made;

(2) To finance a contract to construct or improve, or demolish real property if the agreement provides for a security

interest in the proceeds of the contract; or

(3) To finance the raising or harvesting of a farm crop or the raising of livestock or other animals if the agreement provides for a security interest in any property subject to the lien imposed by section 6321 at the time of tax lien filing, in the crop raised or harvested, or in the livestock or other animals raised.

For purposes of subparagraphs (1) and (2) of this paragraph (b), construction or improvement may include demolition. For purposes of any agreement described in subparagraph (3) of this paragraph (b), the furnishing of goods and services is treated as the disbursement of cash.

(c) *Qualified property.* For purposes of this section, the term “qualified property” includes only—

(1) In the case of an agreement described in paragraph (b)(1) of this section, the real property with respect to which the construction or improvement has been or is to be made;

(2) In the case of an agreement described in paragraph (b)(2) of this section, the proceeds of the contract to construct or improve real property; or

(3) In the case of an agreement described in paragraph (b)(3) of this section, property subject to the lien imposed by section 6321 at the time of tax lien filing, the farm crop raised or harvested, or the livestock or other animals raised.

(d) *Examples.* The provisions of this paragraph may be illustrated by the following examples:

Example 1. A, in order to finance the construction of a dwelling on a lot owned by him, mortgages the property to B. The mortgage, executed January 4, 1971, includes an agreement that B will make cash disbursements to A as the construction progresses. On February 1, 1971, in accordance with § 301.6323(f)-1, a notice of lien is filed with respect to A's delinquent tax liability. A continues the construction, and B makes cash disbursements on June 10, 1971, and December 10, 1971. Under local law B's security interest arising by virtue of the disbursements is protected against a judgment lien arising February 1, 1971 (the date of tax lien filing) out of an unsecured obligation. Because B is the holder of a security interest coming into existence by reason of cash disbursements made pursuant to a written agreement, entered into before tax lien filing, to make

cash disbursements to finance the construction of real property, and because B's security interest is protected, under local law, against a judgment lien arising as of the time of tax lien filing out of an unsecured obligation, B's security interest has priority over the tax lien.

Example 2. (i) C is awarded a contract for the demolition of several buildings. On March 3, 1969, C enters into a written agreement with D which provides that D will make cash disbursements to finance the demolition and also provides that repayment of the disbursements is secured by any sums due C under the contract. On April 1, 1969, in accordance with § 301.6323(f)-1, a notice of lien is filed with respect to C's delinquent tax liability. With actual notice of the tax lien, D makes cash disbursements to C on August 1, September 1, and October 1, 1969. Under local law D's security interest in the proceeds of the contract with respect to the disbursements is entitled to priority over a judgment lien arising on April 1, 1969 (the date of tax lien filing) out of an unsecured obligation.

(ii) Because D's security interest arose by reason of disbursements made pursuant to a written agreement, entered into before tax lien filing, to make cash disbursements to finance a contract to demolish real property, and because D's security interest is valid under local law against a judgment lien arising as of the time of tax lien filing out of an unsecured obligation, the tax lien is not valid with respect to D's security interest in the proceeds of the demolition contract.

Example 3. Assume the same facts as in example 2 and, in addition, assume that, as further security for the cash disbursements, the March 3, 1969 agreement also provides for a security interest in all of C's demolition equipment. Because the protection of the security interest arising from the disbursements made after tax lien filing under the agreement is limited under section 6323(c)(3) to the proceeds of the demolition contract and because, under the circumstances, the security interest in the equipment is not otherwise protected under section 6323, the tax lien will have priority over D's security interest in the equipment.

Example 4. (i) On January 2, 1969, F and G enter into a written agreement, whereby F agrees to provide G with cash disbursements, seed, fertilizer, and insecticides as needed by G, in order to finance the raising and harvesting of a crop on a farm owned by G. Under the terms of the agreement F is to have a security interest in the crop, the farm, and all other property then owned or thereafter acquired by G. In accordance with § 301.6323(f)-1, on January 10, 1969, a notice of lien is filed with respect to G's delinquent tax liability. On March 3, 1969, with actual notice of the tax lien, F makes a cash disbursement of \$5,000 to G and furnishes him

seed, fertilizer, and insecticides having a value of \$10,000. Under local law F's security interest, coming into existence by reason of the cash disbursement and the furnishing of goods, has priority over a judgment lien arising January 10, 1969 (the date of tax lien filing) out of an unsecured obligation.

(ii) Because F's security interest arose by reason of a disbursement (including the furnishing of goods) made under a written agreement which was entered into before tax lien filing and which constitutes an agreement to finance the raising or harvesting of a farm crop, and because F's security interest is valid under local law against a judgment lien arising as of the time of tax lien filing out of an unsecured obligation, the tax lien is not valid with respect to F's security interest in the crop even though a notice of lien was filed before the security interest arose. Furthermore, because the farm is property subject to the tax lien at the time of tax lien filing, F's security interest with respect to the farm also has priority over the tax lien.

Example 5. Assume the same facts as in example 4 and in addition that on October 1, 1969, G acquires several tractors to which F's security interest attaches under the terms of the agreement. Because the tractors are not property subject to the tax lien at the time of tax lien filing, the tax lien has priority over F's security interest in the tractors.

[T.D. 7429, 41 FR 35503, Aug. 23, 1976]

§ 301.6323(c)-3 Protection for obligatory disbursement agreements.

(a) *In general.* Even though a notice of a lien imposed by section 6321 is filed in accordance with § 301.6323(f)-1, the lien is not valid with respect to a security interest which:

- (1) Comes into existence after the tax lien filing,
- (2) Is in qualified property covered by the terms of an obligatory disbursement agreement entered into before the tax lien filing, and
- (3) Is protected under local law against a judgment lien arising, as of the time of tax lien filing, out of an unsecured obligation.

See paragraphs (a) and (e) of § 301.6323(h)-1 for definitions of the terms "security interest" and "tax lien filing." For purposes of this section, a judgment lien is a lien held by a judgment lien creditor as defined in paragraph (g) of § 301.6323(h)-1.

(b) *Obligatory disbursement agreement.* For purposes of this section the term "obligatory disbursement agreement"

means a written agreement, entered into by a person in the course of his trade or business, to make disbursements. An agreement is treated as an obligatory disbursement agreement only with respect to disbursements which are required to be made by reason of the intervention of the rights of a person other than the taxpayer. The obligation to pay must be conditioned upon an event beyond the control of the obligor. For example, the provisions of this section are applicable where an issuing bank obligates itself to honor drafts or other demands for payment on a letter of credit and a bank, in good faith, relies upon that letter of credit in making advances. The provisions of this section are also applicable, for example, where a bonding company obligates itself to make payments to indemnify against loss or liability and, under the terms of the bond, makes a payment with respect to a loss. The priority described in this section is not applicable, for example, in the case of an accommodation endorsement by an endorser who assumes his obligation other than in the course of his trade or business.

(c) *Qualified property.* Except as provided under paragraph (d) of this section, the term "qualified property," for purposes of this section, means property subject to the lien imposed by section 6321 at the time of tax lien filing and, to the extent that the acquisition is directly traceable to the obligatory disbursement, property acquired by the taxpayer after tax lien filing.

(d) *Special rule for surety agreements.* Where the obligatory disbursement agreement is an agreement insuring the performance of a contract of the taxpayer and another person, the term "qualified property" shall be treated as also including—

- (1) The proceeds of the contract the performance of which was insured, and
- (2) If the contract the performance of which was insured is a contract to construct or improve real property, to produce goods, or to furnish services, any tangible personal property used by the taxpayer in the performance of the insured contract.

For example, a surety company which holds a security interest, arising from cash disbursements made after tax lien